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May 15, 1996

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Mr. William E. Kennard
General Counsel
Federal Communications Commission
Washington D.C.

EX PARTE OR LATE FILED

In Re Matter of Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers, C. C. Docket No. 95-185.

Dear Mr. Kennard:

I am writing this letter to you in my capacity as consultant for the Bell Atlantic Companies and SBC Communications Inc.. I have enclosed a copy of a white paper that I have prepared which outlines the takings challenges that I believe undermine the soundness of the Commission's tentative bill and keep proposal governing interconnections between Commercial Mobil Radio Service (CMRS) providers and Local Exchange Carriers (LECs). Over the years, I have done extensive work in both law and economics and in the constitutional law of eminent domain, both generally, and as it applies to rate regulation.

As you know, the Commission has "tentatively conclude[d] that, at least for an interim period, interconnection rates for local switching facilities and connections to end users should be priced on a 'bill and keep' basis." (NPRM, at P. 4). The enclosed white paper analyzes the bill and keep proposal along two separate frontiers. The first asks about the consistency of the proposal with the constitutional mandate of the takings clause. The second addresses the relationship between the bill and keep proposal and the existing case authority. Let me briefly summarize each part.

In dealing with the constitutional issues raised by the proposal, it is best to begin with a single phone call that can be completed only with the cooperation of two companies. It can be taken as given that the interconnections will be established either by private agreement or under FCC order, so that the only question is the distribution of the costs associated with the transmission of the call. The bill and keep proposal states in effect that the party which originates the call gets to keep all the revenue from it, even though the resources of the receiving carrier are used to complete the transaction. Looked at in isolation, this view of the matter surely requires

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regulation of public utilities and require that the rate structure imposed by any given rate order allow the carrier to recover a reasonable rate of return on its original investment. Here it is critical to stress that the key Supreme Court pronouncement in Hope Natural Gas v. FPC, 320 U.S. 591 (1944) required that the just compensation be provided in connection with each individual rate order. That rate order requirement means that it is not possible for any regulator to circumvent the just compensation obligation with an unenforceable assurance that whatever is lost in this proceeding will be made up at some other time. The inability to balance the accounts over time within the FCC, or to balance the accounts between the FCC and the state agencies points out the critical importance of the judicial requirement that each rate order be a self-contained unit, brought to closure at a single time. The bill and keep proceeding has to stand on its own, and the losses that are imposed on the LECs cannot be wished away on the assumption that some future ratemaking procedure will authorize compensatory rates.

The basic framework under the rate of return cases, moreover, is not displaced by the "reasonable expectations" test that has been developed by the Court in Penn Central Transportation v. New York, 438 U. S. 104 (1978). That case dealt with land use regulation, where the scope of state discretion is always greater given the danger of conflicts over land use between neighbors. But the moment the matter becomes one of rate regulation, the clear and justified expectation is that all rate proceedings will provide a reasonable rate of return on invested capital, just as the decision in Hope provides.

As a matter of both theory and case law, therefore, the proposed bill and keep order has to stand on its own when faced with a challenge under the takings clause. Owing to the imbalance in call origination, a bill and keep system works a major redistribution in wealth away from the LECs to the CMRS providers in a manner that is inconsistent with the takings clause of the Constitution.

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